CITY OF TUCSON EMPLOYEES VOLUNTARY DEFERRED COMPENSATION MANAGEMENT BOARD – Meeting minutes from December 3, 2009

Members Present: Joe Barkenbush, Chair
Kelly Gottschalk, Finance Director
Dennis Woodrich, Member
Steven Postil, Member

Staff Present: David Deibel, Board Counsel
Joel Peterson, Risk Management Administrator
Allan Bentkowski, Investment Manager
John Behrens, Finance Analyst
Michael Hermanson, Retirement Manager
Doris Rentschler, Finance Analyst
Michael Jesse, Management Analyst
Claire Beaubien, Retirement Administrative Assistant

Guests Present: Ken Wedemeyer, ICMA-RC
Gary Inorio, ICMA-RC
Walid Rafai, ICMA-RC (via teleconference)

A) Call to Order
Chairman Barkenbush called the meeting to order at 10:03 a.m.

B) Consent Agenda - approval of minutes for September 10, 2009
Dennis Woodrich **moved, seconded** by Steve Postil, to approve the Consent Agenda as corrected. **Motion passed 4 to 0** (Cindy Bezaury, absent, excused).

C) ICMA-RC 457 and 401 September 30, 2009 Quarterly Plan Review
1) Fund watch follow-up

Mike reminded the Board that these four funds have been reviewed and analyzed each quarter for the past year. These funds will be analyzed once again to determine if their performance is up to par or if any or all of them should be considered for replacement.

Walid Rafai from ICMA-RC Headquarters was available via telephone to discuss the various funds' performances. Walid reported that the market has been very volatile over the past 18 months. During that period, there were 4 negative GDP quarters, but the third quarter was positive. Most of the recovery has been attributed to low interest rates, governmental bail outs, and the markets are telegraphing economic activity. Certain market sectors have improved, like Real Estate, even though our area (Arizona) has not recovered much. Emerging markets were hit really hard in previous quarters but have shown improvement and have managed to outpace developed markets, which also rose at a slower rate than they did in the second quarter. The S&P was down nearly 50% over the past 18 months but has now rallied and is currently posting a positive 20%. For the third quarter, the S&P posted a return of 15.61%, but over the annualized past 10 years, it posted a -0.15%. Emerging markets with exposure to natural commodities have done well and because of the weak dollar.

Reviewing specific mutual funds:
a. RiverSource
Walid reported that RiverSource is showing signs of recovering relative to its peers. They invest in small and mid-cap stocks. RiverSource was overweight in energy and industrials compared to their peers, and energy did poorly last year with gas at $4.00/gallon. Other funds positioned for the recovery such as RiverSource positioned themselves too early, which caused their performance to suffer in the first quarter

of 2009. Now, after seeing a recovery start, the company has done well because of their early positioning. Walid reported that for the third quarter, RiverSource was in the 31st percentile. For the one year, RiverSource was in the 60th percentile. Walid commented that many of the funds in the portfolio were favorable long-term but performed poorly for the past year only. They haven't changed anything in the way they do business and have had no change in staffing, so there is no overwhelming opinion on replacement.

A question was raised regarding the inception date for VT Eaton Vance Large-Cap Value, proposed as an alternative, or replacement to RiverSource. The inception date was listed as September, 1931 and Walid confirmed that date was correct. Chairman Barkenbush commented that another alternative to RiverSource was Becker Value Equity, listing a gross expense ratio of 1.23 which is effective through February 28, 2010. Chairman Barkenbush inquired if that date was negotiable or was if it was a fixed date. Walid replied that date was fixed and could not be changed. He then asked the Board if anyone had any interest in replacing RiverSource with one of the alternatives offered by ICMA-RC. There was no response by the other members of the Board.

b. Ranier Small/Mid Cap Equity

Walid reported that Ranier posted a performance in the 16th percentile in the third quarter. Last year, Ranier was overweight in financials and industrials which hurt their performance. Ranier invested in small-cap growth companies more than its peers and last year's performance was impacted by their investment in small-cap growth companies. Ranier is focused on high quality stocks in terms of capitalization and balance sheet quality. Their focus on such high quality stocks has not been rewarded during this rally. This has hurt their performance as well. Pundits call the rally a "low quality" rally and stocks that have been hurt the most came back the best. Ranier is the only fund in the mid-growth box leaving no alternatives from that style box. Ranier had negative returns in the one year and three year periods, posting in the 98th percentile for one year, 82nd percentile for the three year. The ten year rating was in the 18th percentile.

Walid then discussed possible replacement stocks for Ranier. He began with Columbia Acorn, explaining that their long term track record was very favorable. This fund has less volatility than Ranier. The standard deviation of volatility for the one year is much higher than the three year or five year postings due to the past year's performance and reflecting what has been happening in the capital markets. The fund holds about 300 positions and doesn't take major bets. It will hold itself in a down market better than most other stocks but when the market rallies, this stock will not be a top performer. Times Square Fund does not have a very long track record but it is favorable. This fund is more expensive than the other alternative choices. T Rowe Price Mid-Cap Growth fund has performed very favorably. This fund has outperformed the category average and the Russell Mid-Cap Growth Index. Their gross expense ratio is less than the Ranier fund and the net expense ratio is the same. Chairman Barkenbush asked if the management team has changed or if it remained the same since inception. Walid replied that the team has been around for a long time, 17 years for the portfolio manager, Brian Bergus. The fund has a high quality focus and may lag where the market is an explosive growth or a speculative growth taking place. Ken Wedemeyer asked Walid if T Rowe Price Mid-Cap Growth will have more mid-cap stocks than the small-mid cap Ranier. Walid replied that their average market cap is $5.1 billion while Ranier's average market cap is less than that at $2.2 billion. Ranier would have more exposure to small-cap stocks than T Rowe Price Mid-Cap.

Steve Postil commented that he believes that Ranier needs to be replaced and it is just a matter of determining with which fund to replace it. This fund is not doing well and there is a lot of participation in it by the membership, so his opinion is that it needs to be changed. Allan Bentkowski remarked that he believed that there has to be an overwhelming reason to change a fund out and not just because a fund's performance is poor for a period of time. If the long term track record of Ranier is analyzed compared to the alternatives, Ranier has outperformed. He said that looking at the -17.11% return posted by Ranier, he would be more inclined to invest in that stock because of the likelihood that it will rally significantly. He said that it isn't a good practice to chase returns and, long term, Ranier has outperformed the alternatives being offered. Ken offered an alternative suggestion that there was no reason that a fund couldn't be added to the lineup. While it has been the City's goal to streamline the fund lineup, another fund could be added.

Other alternatives for Ranier:

- Columbia Acorn fund performs a combination of fundamental research and looks at companies that have a lower valuation. They look for companies with favorable positions versus their peers. They have approximately $11 billion in assets, managing over 350 companies. They are contrarian in outlook with a 21% turnover. Their largest sector is in financials at 14% and then healthcare of 11.5%. They have approximately 11.6% in their top ten holdings.

- T. Rowe Price has 141 positions with 33% turnover. They have approximately $531 million in assets. Their largest sector weighting is in healthcare at 17%. They have approximately 18.5% in their top ten holdings.

Ranier has 131 holdings as of 6/30/09, with 127% turnover. They have approximately $1.8 billion in assets.

Following and overview of alternatives, the discussion turned to the next funds to be reviewed:

c. Third Avenue Value

Walid reported that Third Avenue is now doing well since it has been recategorized. Their long-term performance has been very favorable.

d. Legg Mason Emerging Markets

Legg Mason's long term performance has been favorable in the three, five and 10 year rankings. Legg Mason has two layers as part of their investigative process, a quantitative layer and a fundamental layer. They look at the stocks with a bottom up approach. Legg Mason has 240 holdings with a 71% turnover rate. Twenty percent of these holdings are in the top 10 holdings. Legg Mason has $277 million in assets. However, they were at the 84^{th} percentile of their peers for the one year chart; in the 3 year category, they were in the 35^{th} percentile and 14^{th} of their peers for the 5 year category. The problem is, their performance was worse than any of the other prospective replacement funds. Their assets are much smaller than the prospective replacements, as well and they have underperformed significantly in the one, three, five and ten year returns compared to their peers and their index. The return for the one year versus their benchmark was 6.67% versus 19.07% for the MSCI EM NR USD. The Board decided that that Legg Mason's short term and long term performance was not in line with the Board's investment policy and should be considered for replacement.

Alternatives to Legg Mason

- Lazard Emerging Markets that uses a bottom up approach in stock selection. They look for stocks that are relative value, not necessarily deep value. They look for stocks that appear to be cheap on a relative basis using return on equity. They have 72 holdings as of September 30, 2009 with 31% in their top 10 ten holdings. Their turnover is 43%. Lazard has $3.3 billion in assets.

- Oppenheimer Developing Markets Fund. The fund's stock selection has 127 holdings as of 8/31/09 with 28% of these holdings in the top 10 holdings. They have a 55% turnover rate. Oppenheimer has $6.8 billion in assets.

- RS Emerging Markets has $985 million as of 9/30/09. They have 25% of their portfolio in their 10 ten holdings. They have approximately 87 holdings. They have co-portfolio managers. They are also bottom up driven. They have 62% exposure in Asian Pacific and this helped their performance. They have 82% turnover.

e. Other Funds

Fidelity Diversified International - Long term performance for Fidelity has been favorable while the five year and three year performance has been impacted by their one year lagging performance. For the one year performance, they were in the 78th percentile and the three year performance rating was 69th percentile. They were underweight to emerging markets, specifically in Japan. Because of the appreciation of the yen and the underweight in Japan, their performance suffered. Also, they were impacted significantly by the financial crisis last year. Their performance for the 3rd quarter is in the 52nd percentile which has improved but is still only average. This fund is overweight in developed markets which have not done as well as emerging markets. They have since increased their position in Japan but it is still below the MSCI EAFE Index. This fund has nearly $31 billion in assets. After visiting with this company, ICMA has no concerns regarding this company's underperformance.

Walid discussed the Oppenheimer International Growth Fund. While Fidelity has 350 names, Oppenheimer has approximately 146 names in their portfolio. Oppenheimer has $1.3 billion in assets. Oppenheimer looks for stocks with themes such as aging or restructuring and tries to gain exposure to companies that will develop and capitalize on that theme in the next 3 – 5 years. Their turnover is 21% while Fidelity has a 58% turnover. Oppenheimer is willing to trim their positions and take profits in some of their positions if they become extended on the upset. They would also gain exposure to smaller caps and emerging markets. Fidelity has more focus towards developed countries. Oppenheimer has approximately 7% of their portfolio in emerging markets. Fidelity has only 5% of the portfolio invested in the emerging markets.

2) Review of Fund Line-up

a. Investment Funds considered for Removal

Steve Postil **moved, seconded** by Dennis Woodrich, to add the Columbia Acorn fund to the fund line up and not eliminate Ranier from the line up. Kelly Gottschalk asked Steve to explain why he was more in favor of Columbia Acorn instead one of the other alternatives. Steve replied that the 10 year return was attractive and their difference in style and size was attractive and gives the members a clear choice. **Motion passed 4 – 0.**

Steve Postil **moved, seconded** by Dennis Woodrich, that put Fidelity on the watch list for another quarter and add the Oppenheimer International Growth Fund to the lineup. **Motioned passed 4 – 0.**

After reviewing Legg Mason and the alternative funds that could replace Legg Mason, Chairman Barkenbush asked the Board if they wanted to change any of the line up as far as Legg Mason or the other funds that were on the watch list were concerned. Dennis Woodrich **moved, seconded** by Steve Postil, to replace Legg Mason with Oppenheimer Developing Markets. **Motion passed 4 – 0.** Gary Helm advised the there is a redemption fee of 2% or has to be held for 60 days before redemption to avoid the 2%. Therefore, all transactions going to Legg Mason needs to be stopped so that the requirements can be fulfilled.

b. Replacement Fund consideration

Allan Bentkowski asked why it isn't a voluntary option for the participant to continue to participate in a particular fund even if the Board has decided to replace it. He said he thought it might be an administrative issue but there are funds he would rather stay in instead of going with the replacement fund. Ken replied that the Board would have to continue oversight of a replaced fund and then decide if it is a good fiduciary action to allow participants to contribute to a documented fund that has been performing poorly.

c. Timeline for removal and replacement

Gary reminded the Board that there is a 60+ day window required in order for any changes to occur, so these changes won't occur until March, at the earliest. Notification will be sent to participants in these funds to notify them of changes made and what they need to do when the changes take place.

D) Election Committee

Steve Postil reported that Marie Nemerguth and Peter Gavin agreed to serve on his committee. While Dennis Woodrich's term is expiring in January, 2010, he is eligible to run for re-election, according to Board Attorney, David Deibel. Solicitation letters would be sent out near the end of December, with a submission deadline a few weeks later.

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E) Educational Program – Final summary of 2009 plan year activity

Gary reminded the Board that at the last meeting it was approved to allow ICMA-RC to conduct fewer group meetings than were specified in the original contract. Instead of conducting 120 group meetings, 70 were agreed on. 78 group meetings were actually conducted. Other goals were met: the number of individual participant consultations increased to 456. Individual enrollments went down with 131 enrollments for deferred comp. and 25 enrollments in the Roth IRA which was launched in 2008. In 2009, the enrollments dropped significantly. There were 311 enrollments in 2008 and an average of 320 -350 over the past few years. There have been 800 new enrollments in the plan since ICMA-RC became the sole provider.

Gary reported that the number of roll-ins were down for 2009 at $5.5 million level. Previous years showed approximately $8 – 9 million range. This follows a trend that is visible with other areas of the plan, such as lower participation rates, and lower enrollments.

CFP Services have had successful results, with the best attended seminar entitled "How Much Will Retirement Cost?" Gary discussed the National Save For Retirement Week event held at the City. He said it tied in well with ICMA-RC's "It Pays To Save" program. Although the participation was low, the dissemination of information was much better than in previous years.

Going forward, Gary listed various items that they plan to improve participation/enrollment in the Plan. They plan to establish an open enrollment only office hours at various departments on a monthly basis – emphasizing the need to enroll for retirement saving. They plan to increase the frequency of visits of the Certified Financial Planner, Tom Axline, to every six weeks thereby presenting 16 seminars. They will also plan to mail surveys to select participants regarding service levels, what they desire from a retirement plan provider and gauge their overall satisfaction with ICMA-RC services. They will present a "Retirement Readiness" Campaign targeting participants who are at or near retirement age.

Presentation topics will be changed to meet the current needs of the participants. One of the topics to be discussed will be "Money and Credit Matters" which is great for the current financial environment with people struggling to meet their financial obligations. Other topics to be discussed are: "Getting Started in your 457 & Roth IRA Plans"; "Saving Toward Your Retirement Dreams"; "Transitioning into Retirement" for the first CFP seminar.

F) Status of Customized Survey

Ken commented that a specific survey was conducted to discover who is participating and who is not and, if they are participating, are they getting what they need from ICMA-RC. He said that they use a company called Belarus Survey that allows a customization of the survey needed to cull the information received so that an appropriate analysis can be made to determine what is missing and what is needed. Also, a postcard will be sent to non-participating employees without email to find out what can be done to encourage them to participate. This research project will be conducted in the next quarter.

G) Review of Fee charges

1. Summary comparison for past two years
2. Review of Administrative allowance account activity for past year
3. Consideration of fee returns to participants

There is $166,000 in an accumulated administrative allowance part of which ($50,000) goes to the Tucson Supplemental Retirement System for the cost of administering the Deferred Compensation Plan. As background, the money that accumulates in this account is what exceeds the revenue commitment made to ICMA for the cost to run the deferred compensation program. After administrative costs are deducted, the balance is intended to be returned to participants' accounts. A total of $116,000 will be returned to participants with balances as of 9/30/09. Last year, $93,000 was returned to participants' accounts. Steve Postil **moved, seconded** by Dennis Woodrich, to transfer $50,000 to TSRS for administrative costs for the Deferred Compensation Plan and refund the balance of $116,000 to participants with account balances effective 9/30/09. **Motion passed 4 – 0.**

H) Plan Document Implementation

1. Discuss status of implementation

Mike reported that a resolution to Mayor & Council was successfully submitted to amend the plan documents of the 457 and 401 plans. These plans are now up to spec with changes made by the IRS in the past 3 years, no further issues to report.

2. 401 Enrollment Report

There were two announcements made regarding 2009 being the final year of enrollment for the 401 (a) Retirement Supplemental Savings Plan. There was some activity after the first announcement was made just prior to November 1, 2009. After the reminder notice was sent out, a flurry of activity followed, and has so far resulting in 16 enrollments.

I) It Pays to Save Campaign

Ken announced that the next flyer would be distributed in January, 2010. It was recommended that, since Mary is visiting most departments, she could take flyers with her to request they be posted and notice whether other flyers have been posted. Doris suggested an expiration date be put on the flyer so the departments know when they can be taken down and/or replaced with the new flyer.

J) Selected Plan Statistics – 457 Plan

Ken reported that there has been a drop in contributions, down nearly 30% from 2008. The average bi-weekly contribution has dropped approximately 28%, as well. Ken conjectured that approximately 80% of the group are active participants unable to save at this time. There was also a drop in active participation is 10% which was typical across the country. Ken commented that there should be an educational session on diversification.

K) Report on National Save for Retirement Week

Mike commented that pictures of National Save for Retirement Week activities for the City of Tucson were included in the board packets. A baseball theme was used this year and each participant was given a base runner card so they could go from base to base getting information regarding their retirement prospects. Ken commented that some of his other clients are going to copy our idea for next year.

L) Summary Plan Statistics

Mike indicated the report compiled that provided statistical information on various aspects of the plan such as loans for the Board's review. Included in the report were contributions by age groups, average bi-weekly deferral, number of members receiving distributions, etc.

M) Call to Audience

None heard.

N) Adjournment

Steve Postil **moved, seconded** by Dennis Woodrich, to adjourn the meeting. **Motion passed 4 to 0** (Cindy Bezaury, absent, excused)**. Meeting adjourned at 12:40 p.m.**

Approved:

Joe Barkenbush	3-12-2010		03-12-10
Joe Barkenbush Chairman of the Board	Date	Michael Hermanson Retirement Administrator	Date